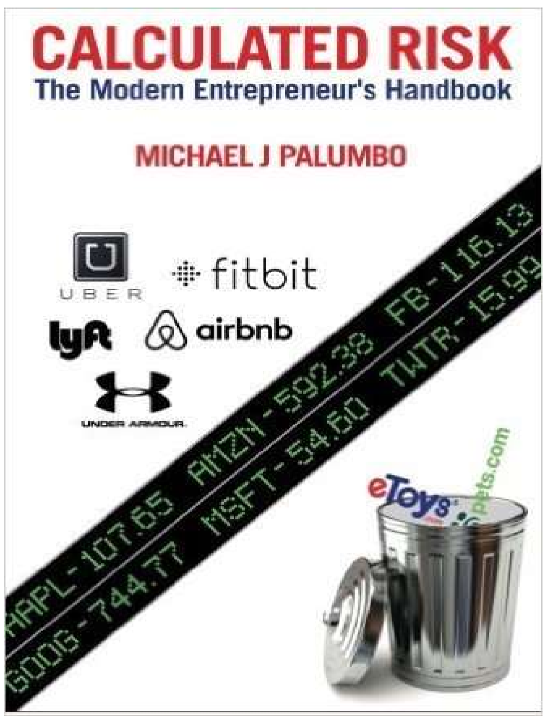
**Two decades ago Michael J. Palumbo, ranked as one of the 100 top traders in the world, launched Third Millennium Trading at the Chicago Board Options Exchange. Less than 10 years later his $250,000 investment was worth in excess of $100,000,000. He then became the angel investor in a fintech firm, GETCO, and exited when the start-up was valued at over $1.7 billion. He now reveals how today's wannabe entrepreneur can develop a raw idea and turn it into a rich opportunity, sharing along the way his monumental success story in a new book:**

# Calculated Risk:

## The Modern Entrepreneur's Handbook




How does an entrepreneur take any idea and turn it into a profitable venture? What do investors look for when evaluating start-ups?

These two important questions are answered in a new book by one of America's top traders, Michael J. Palumbo, called ***Calculated Risk: The Modern Entrepreneur's Handbook***. The book helps founders and executives navigate today's business climate from idea conception through funding, expansion, and exiting.

*Calculated Risk* provides an insider's perspective from someone in the know. Palumbo started a prop trading group in Chicago that turned into a highly successful U.S. stock options business, a firm that was one of the largest equity options trading groups in the country in the late 1990's and early 2000's.

**<u>Palumbo's book reveals the following:</u>**

- How to launch an idea from concept to funding.
- How to best hire and build a start-up – right until you exit.
- What venture capitalists look for in a start-up –and why it is not always profitability.
- What start-ups should look for from their investors – it is not always about the money.
- Why the best entrepreneurs are the ones who can predict what people will need before they even know they in fact need it.
- How some entrepreneurs can gain an edge over their competition.

Palumbo has a tell-it-like-it-is approach to revealing insights in the marketplace on how things will shake out. Offering a voice of experience and vision, Palumbo not only explains why something is happening in the markets, but also reveals why something will happen.

**<u>Palumbo is available to lend insight on the following</u>:**

- Coming trends that will impact the markets, including political, technological, and financial ones.
- Why he believes Trump will win but his presidency won't impact the markets significantly.
- How a high-risk approach to the markets can net you a big pay-off.
- The role speed still plays in the transaction of trades – and how he made over a hundred million dollars simply by being faster than everyone else.
- How to identify which start-ups investors will back – and why.
- Determining if you have what it takes to be an entrepreneur.
- What the best predictors of future market trends and global macro-events will be.

Featured in a VH1 documentary on Wall Street billionaires, as well as a *CNBC-TV, Crains*, and *Trader Monthly Magazine*, Palumbo offers his unique take on the forces and events that shape today's markets.

He calls upon examples of what to do and not do from Facebook, Uber, Amazon, eBay, Apple, and other popular companies.

"Starting a company is without a doubt one of the most challenging things you can do in your life," says Palumbo. "If successfully done it can also be one of life's most rewarding accomplishments as well. What I have tried to do in this book is cover the entire adventure from getting your idea and how to know it is an actionable one, all the way until you are looking for a partial or full exit from the business."

*Calculated Risk* highlights Palumbo's success of starting his own firm from scratch and how it grew into a big hit. The book showcases the truths and strategies that actually worked for him and could for others.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# Michael J. Palumbo
## <u>Biography</u>

Michael J. Palumbo turned a $250,000 investment into a company worth well over $100,000,000. The former Chicago Board Options Exchange floor trader is an entrepreneur, venture capitalist, and the author of the new book, *Calculated Risk*.

Palumbo, 49, is the founder and controlling partner of Third Millennium Trading, LLP, Third Millennium Trading, LLC and TMT Investments, LLC, all Chicago-based proprietary trading and marketing firms.

He is also the principal of MJP Capital, LLC, a private, mid-west regional holding company focusing on both real estate and technology. The two main ventures of MJP Capital are Ceres Acquisitions and Ceres Tech.

In 1996, Palumbo founded Third Millennium Trading LLP on a quarter-million-dollars. Within a decade, it was worth over $100 million. He then provided initial funding as the original venture capitalist for the high-frequency trading firm GETCO. That firm was valued at $1.7 billion when he exited it to a private equity group.

*Crain's Chicago Business* recognized his accomplishments and trading income in its 2005 "40 Under 40 Focus." He was additionally listed among the top 100 traders worldwide in *Trader Monthly Magazine.* Palumbo was also featured in a special VH1 television documentary, "The Fabulous Life of Wall Street Billionaires – Ballers" and a book, *Trade With Passion and Purpose*. CNBC-TV *Power Lunch* called Palumbo "unusual" and "highly-intelligent, highly successful, and a big risk-taker" during an interview with him.

Palumbo began his career as a credit analyst at Duff & Phelps, where he analyzed the bond insurance industry. He then started his CBOE floor career as a clerk for Susquehanna Financial Group in 1993. During his employment at Duff & Phelps, Palumbo created one of the first stress test models for bond insurance using Monte Carlo Simulation.

In 2000, Third Millennium Trading, LLP was one of the largest volume equity-market-making trading firms in the world. Mr. Palumbo's specialty is the equity options market, where he trades on macroeconomic factors, rarely holding a position for more than a month.

He received his Bachelor of Science in Management Information Systems from Illinois Institute of Technology in 1988. He then completed his Master of Business Administration in Finance and Economics at Northwestern University in 1990 at the age of 23.

He resides with his wife and newborn twins in the Gold Coast neighborhood of Chicago. He has four children with his first wife. For more information, please consult: www.michaeljpalumbo.com.

# Michael J. Palumbo
## *Calculated Risk*

1. **Michael, what inspired you to write *Calculated Risk*?** I felt it was time to take the experience I had collected and finally put it down in writing. I knew I had a lot to offer to young entrepreneurs who were looking for a methodology for starting businesses. Between the companies I had started, backed and invested in, I knew I had a lot of experience that people would find valuable.

2. **How did you manage to parlay a small investment into a megadeal?** I did it twice. Once was turning my own trading company into an industry leader starting with just $250,000. Then I later invested in a high frequency trading firm and turned a $750,000 investment into over $100 million in eight years. My trading firm was built because I recognized a need in the options market for a one-stop shop to get an options market in any US equity. I provided these markets quicker and with more liquidity than my competitors so we grew very quickly and became one of the biggest options trading firms in the country from 1998-2008. The investment in the HFT firm did well because I picked a great bet on two very driven founders who were way ahead of the market as far as technology. They executed very well with my help and the firm was partially purchased by a private equity firm eight years later with a valuation of $1.7 billion.

3. **Why do you feel the United States has a strategic advantage over what you call commodity-based countries?** Because the US is a technology based economy, in an era where technology is causing deflationary pressures on commodities. The balance of power is with technology-based economies now, as it usually is, and looks to stay that way for the foreseeable future.

4. **What are some things company founders should look for in building their organization with new hires?** 1. Are they technically capable in the area for which they will be responsible? 2. Are they morally sound? 3. Can they be incentivized to work at an extremely high level? 4. Will they remain loyal if given reasons to do so? 5. Are they able to work on a team?

5. **What types of questions should be asked of these prospective employees?** Depends on the type of job. I ran a trading company and the most important quality of an employee was the ability to make quick accurate decisions with limited information. Therefore IQ type questions were very good in identifying good candidates. Sales type jobs would require questions that identified a person's charisma. Tech jobs would require the applicant to exhibit their expertise in the specific technology such as programming.

6. **When seeking investors, what should a company be looking for?** Keeping it short and sweet, you want investors who:

- Are good, honest people.
- Offer a deal that has fair terms and pricing.
- Have the ability to open doors, help grow business, give you solid advice in sticky situations, and importantly, are people who actually want to (and will take the time to) help.
- You like as people and can see yourself having a positive relationship with.
- Are willing to tell you when things are not working and help get your company on the right road to success, and do so in an agreeable manner.
- Are easily accessible when you need guidance.

7. **What terms are simply unacceptable when lining up funding?** It is important for entrepreneurs to have a good understanding of the valuation of their firm. The biggest deal breakers are either too low a

price being bid, and also having the bid come from a person or group that the founders do not feel they can work with. I feel a lot of founders sell their stakes too cheaply because they want to get funding and end up regretting it later. Or they begin a relationship with VCs who they later have difficulty working with and so those are the mistakes I caution founders to look for.

8. **What advice would you give to the entrepreneur of 2016?** Figure out what the world needs that it doesn't have and then be willing to work 100 hours a week to get that to the world as efficiently as possible. Entrepreneurship is a life style choice and it doesn't come easy nor does success follow the lazy. Even with a great idea you have to have the intelligence and drive to make it happen.

9. **Why do you believe being an entrepreneur is a learnable process?** Because just about everything is a learnable process. You just need someone who has made enough mistakes and done some good things as well to formulate that process.

10. **When should one contemplate an exit strategy?** The best time to exit is when pricing is at a premium for your company. Also, if you believe the competition will begin to change the value of your firm for the worse. Bottom line is sell high, at a time when there may be some irrational exuberance. Also obviously if you are getting to a point where you do not feel you are the man for the job anymore. That is often hard to see but wise people can do this. Sell to a buyer who can take your company to the next level.

11. **What is the ideal way to leave a company one started from scratch?** Any one of the ways I describe in the last question. Either at a high point in your firm's pricing, before competition starts to emerge or become visible to the marketplace, or to a group who can take the firm to another level that you maybe cannot do on your own, due to that buyer's connections or competitive advantages, including maybe superior technology.

12. **Which presidential candidate promises to be more beneficial to helping entrepreneurs flourish?** Trump has been an entrepreneur his whole life, Clinton is a career politician. My bet would be on the entrepreneur.

13. **In your book you predict Apple Watch will not be successful in the long term. Why?** How challenging is it to prognosticate where a company will be in five years? The watch does not bring anything new to the marketplace. It already is showing signs that I am right given how Apple's stock has performed in the past couple months. Apple makes money when it gives people something new that they need. The watch will be a bust. Predicting where a company will be in five years becomes more challenging the higher its current growth rate and the less history it has. Just like predicting anything, the less data you have and the more volatile it is, the harder it will be to predict its future. The key is not predicting it perfectly, the key is predicting it better than others do.

14. **What do capitalists really look for when valuing a start-up?** The first things they look for is earnings and growth. If the firm has both than it will be valued highly. With only one, valuations will either be low (if the firm has earnings but no growth), or very difficult (if the firm has growth without earnings). The key to valuing this last group is to predict sales and then assume a level of future profitability once the sales get to a higher level. A good example of this group is Amazon. It has high growth but low earnings. The market loves the company because it understands that Amazon will be able to earn much higher profits whenever it decides to reduce its research expenses and is content that it has solidified its already huge competitive advantage. When that happens, Amazon earnings will get much higher and the market knows this and gives it credit for having this ability to increase earnings when it sees fit.

15. **Why do you believe oil prices will remain lower?** Technology will keep it low. Between fracking and alternative energies, a great amount of added supply has entered the energy markets and it is a situation

that is not going to go away. Certainly demand will continue to increase but it appears technology is creating more sources of energy at higher quantities than the pace of growth in demand. This should keep energy prices low versus the past decade when there was a fear that supply would not be able to keep up. As always happens, entrepreneurs saw an opportunity and have reacted and this should keep prices low for the next 10 years and maybe much longer.

16. **In the past technology may have displaced some jobs but created entirely new ones. Why do you feel that may not be the case moving forward?** Because this time technology is taking away jobs that required much more talent. These high value added jobs when gone are harder to replace with other high value added jobs. So unemployment rates have come down during this recovery but the jobs that are available do not offer as high a pay. So the quantity of jobs has recovered but not the quality. This can change as hopefully technology develops entire new industries that we cannot imagine as of yet, but the way things look for now, we are in a low real wage growth, poor job market period and it does not look like it will change for a very long time, maybe not for a generation or two at least. I hope I am wrong but it does not look good for young people who may for the first time not enjoy a higher standard of living than their parents in developed nations. In developing nations like China, young people should do better than their parents because of how poor their parents have been.

17. **How does one know if they truly have a good idea for a thriving business?** The best ideas solve a large need on the marketplace. It takes into account where the current marketplace is heading and anticipates coming technological innovations. It appeals to as large a group of people as possible so it will have a huge possible market. Finally, it must be feasible given technology as it is and will be in the near future. This is why online shopping failed in the 1990s but is now succeeding. The technology was not available yet in the nineties for an enjoyable online experience.

18. **What role does technology play in the viability of startups investors are seeking to evaluate?** Depends on the industry but usually technology is the primary source of a firm's competitive advantage. Technology is usually what determines which firms lead their industries. It can give you a quality advantage and a cost advantage.

19. **Why do you say that investor and VC guys like you are not looking for profitability when evaluating whether to invest in a start-up?** VCs realize that profitability is usually very difficult in the early stages of a startup. We look for other forms of growth that I call "traction." We want to see huge user bases, growth in revenue, signs that profitability will eventually come. Facebook was not initially very profitable but once it figures out how to monetize its massive user base, its valuation soared. The key is to realize this pending monetization before others do so you can better value these firms.

20. **How can a business take into account where the current market place is heading and anticipate coming technological innovations?** This is just a matter of paying attention and keeping up with current trends. Being a voracious reader is often a characteristic of successful leaders of companies because they have to be able to spot trends that will affect their industries before their competitors do.

21. **What trends do you see impacting Wall Street in the near or long-term?** Fintech promises to change the way business is done on Wall Street but I expect the bankers to be smart enough to buy the best firms before they get innovated out of business. Certainly the area of payments systems such as the promise of Bitcoin will result in simpler, cheaper and faster payments systems, but it is unclear if Bitcoin itself will be the standard or if it will just be the first innovation and then get pushed aside for better alternatives. I do not believe that financial jobs will move from New York and to a lesser extent Chicago. I believe that Wall Street will buy the technology they need and also shape the way this plays out because of their political connections and sheer size.

# Finding Investors
## by Michael J. Palumbo

Not only can it be the most overwhelming aspects of entrepreneurship, but it can also be one of the most dangerous as well. Find the wrong investor and your company could sink in the future due to bureaucracy, hurtful guidance, investor-related pressure, potential misunderstandings and lawsuits, or in the worst case scenario, loss of control of the company you have worked so hard to build.

One thing to remember is the more an investor brings to the table – besides money – the more you should be willing to give up. Find a deal that does not give away too much of your company

**Investors You Want on Your Team**

A. Are good, honest people.

B. Offer a deal that has fair terms and pricing.

C. Have the ability to open doors, help grow business, give you solid advice in sticky situations, and importantly, are people who actually want to (and will take the time to) help.

D. You like as people and can see yourself having a positive relationship with.

E. Are willing to tell you when things are not working and help get your company on the right road to success, and do so in an agreeable manner.

F. Are easily accessible when you need guidance.

Foremost, does the investor have a track record of successfully investing in startups, and can they say how they actually helped the company along the way? Or does the investor have a history of investments ending up in failure or legal battles?

What does the investor's personal life look like? Do they have the ability to focus their energy on helping your firm, or is their focus on other areas not related to your business?

It is important to understand that most often friends and family will likely not understand the risk of the business because they are not tenured, accredited investors. Basically, if they don't understand the risk, your business relationship could quickly become very stressed, and I hate to say it, but even possibly unmanageable. It is important to keep friends and family's investments to a minimum.

Lastly, stay away from investors who upon funding your company will expect you to hire their brother, uncle, niece, and nephew. Using their investment as leverage to fulfill their own needs (employing their family) is a bully technique and not good for your company.

# 5 Questions To Building Your Dream Company

There is an old saying that states if you are the smartest person in the room, then you are in the wrong room. This could not ring any truer than in evaluating candidates to work for your company.

Every employee you hire must be looked at as an investment, and anyone you have to fire or who leaves to join a competitor is a failure on your part to accurately evaluate them at this stage – the time *before* you hire them. And remember, your first few hires will shape your firm possibly as much as you will, so these decisions are crucial ones. Ask yourself these questions when recruiting talent:

1. **Are they technically capable in the area for which they will be responsible?** Some of the best employees I have ever hired did not go to Ivy League schools, and did not have prior experience in the exact task I wanted. What they had was the ability and willingness to learn what they had to in order to be successful. The next step is to evaluate their technical competency through the interview process. In order to do so, you must know what skill set you are after. So to summarize this first test: know what you want in this employee, use a resume only to eliminate candidates who are obviously not qualified, then develop a set of questions that help you quantitatively and qualitatively evaluate your best candidates for the skill set you need.

2. **Are they morally sound?** Literally it comes down to looking that candidate in the eye and asking yourself, "Can I trust them?" At some point during the interview process you should spend time with this person away from the office. I would suggest your final interview stage should be lunch or dinner and a drink out, and it should last a few hours.

3. **Can they be incentivized to work at an extremely high level?** Is this candidate someone who is driven to succeed? Is he or she going to push themselves beyond what they thought were their limits if properly incentivized? I love to hire people who have had success in sports, not because I want a bunch of jocks around my firm, but because they often know how to work on a team, and importantly they are often driven to succeed if proper goals are given to them.

4. **Will they remain loyal if given reasons to do so?** Is the candidate in it to win it, or is this just another job for them? Each employee is an investment of money but often more importantly, of a large amount of time as well. You do not want to help a person develop a large valuable skillset only to see them walk a year or two later to go use it for someone else. Incentivize employees so they remain happy and loyal. Pick people who will stick with your firm if you treat them well.

5. **Are they able to work on a team?** A group of employees that is able to work well together creates a synergy, making the entire firm worth more than the sum of its individual parts (employees). So look for candidates who have shown past work in a team environment, whether it is sports in college or high school, or past teamwork necessary in former jobs. This is important as a team needs members who work well together.

Your employees determine how your company is viewed by the outside world and your customers. Happy employees are a must in a fast-growing firm. This is why that selection process is so important. You must pick them wisely and then make sure you incentivize your employees to help them perform at their best. Incentive programs must be geared to pay off the most when performance is exactly what benefits the firm best.

# Do You Have A Great Idea?
## by Michael J. Palumbo

In 2000, I hedged my company by being the original venture capital investor in the high frequency trading firm GETCO. Trading execution via computers was quickly becoming the new standard at the turn of the century. GETCO had identified the need for even more speed – electronically. In essence, I hedged my own company, betting on a company that developed a technology that would increase speed and liquidity even more. The bet paid off as GETCO became a massive success. By the time GETCO was sold to private equity, the little company I had backed with just $750,000 at a valuation under $5 million grew to over $1.7 billion in a period of eight years. How do you know if you have a good business idea?

1. **Is There A Need?**

A truly great business idea takes into account where the current marketplace is heading and anticipates coming technological innovations. Moreover, great ideas usually give the world something it did not even know it needed. The world maybe had an itchy feeling there was something that could be better, but the new idea had not come into existence just yet. Once this new idea is deployed though, the world cannot live without it. In addition, it is so very important to look at technology not where it is now, but where it is going to be five years from now, when your company is actually up and rolling. The question is: will your idea still be relevant?

2. **The Geography Test**

Next up in evaluating any business idea is what I call the Geography Test. Basically, when entrepreneurs come up with a great idea they often fail to ask themselves how relevant the idea is on a mass scale. In other words, the idea was not only timely and relevant, but also hugely needed and scalable.

3. **The Feasibility Test**

When the idea is great, but revenue, or some other type of growth-related metric, is not there, something under the hood is likely broken. Unfortunately, all too often it is not the idea; it is management. Investors and venture capital guys like me are not looking solely for profitability. Sometimes, we are hardly looking for any profitability at all, especially in startups seeking seed funding. What we are looking for are metrics that show some type of traction. Traction is the key word here. Increasing revenue, rising subscriber-base, organic user-growth – these are all things that offset profitability. Another aspect of the Feasibility Test is determining whether adequate technology infrastructure exists, while also questioning whether the world is ready for the concept as well.

4. **The Competency Test**

You should ask yourself one final question: "Am I the right person to make this happen?" This is a very important part of the idea equation. And you must answer this with complete honesty. You must do what many people find very difficult and go outside of yourself to evaluate your skills, your passion, and ultimately your level of competency for this task. The hardest person to criticize and evaluate in life will always be yourself, and those who truly understand themselves and their skill set are some of the wisest people around. Can you take this idea and make it a reality? What are your skills that uniquely qualify you for this task? And importantly, are you *passionate* about his project?

# 6 Trending Insights & Observations

Michael J. Palumbo, identified as one of the top 100 traders worldwide, has experienced years of profits that sometimes hit the nine digits. He has seen other years, especially during The Great Recession, that were far less profitable. Where does he see the marketplace heading?

In his new book, *Calculated Risk*, he shares his thoughts about technology and its effects on future macroeconomic conditions, including these:

1. **Era Of "Peak Oil" Is Over**
Oil will stay low in the coming years. "In the past any significant drop in oil prices was temporary and oil reloaded to new highs only a few short years later. But I believe this time it is different," says Palumbo.

2. **Tech Is Costing More Jobs Than It Created**
It used to be that for every job lost due to technological change, another was gained of higher pay values. "For the first time in history, innovation in artificial intelligence seems to be making human tasks obsolete at a faster rate than it is creating new tasks," says Palumbo. "This time, technology and entrepreneurs may be causing unemployment and underemployment to rise, and this trend may continue for the foreseeable future."

3. **This Era Doesn't Put A Premium On Commodities You Dig Out Of The Ground**
"Countries that depend on commodities will continue to struggle for the foreseeable future," says Palumbo. "This is why you see countries like Russia and Brazil in depressions, while the United States is able to continue to grow, albeit slowly."

4. **America Is Still The Center Of Entrepreneurialism**
"The current business climate puts a premium on technology," notes Palumbo. "Nations that lead the world in technology will have a comparative advantage that is hard to beat and the United States appears well positioned for this new world."

5. **Apple Watch Is Not A Big Win**
"At the end of the day, the Apple Watch in its current state does not disrupt the industry, and it is really just a less capable smartphone with fitness and medical possibilities on your wrist, in a world where people already have smartphones," says Palumbo. "And it costs at least $349, much more than comparable or even superior models that focus on health and fitness."

6. **Today's State of Entrepreneurialism**
"Entrepreneurialism in the modern age requires that all aspects of business continually focus on acquiring customers/users, while remaining competitive to retain and grow revenue," says Palumbo. "Small companies who are not cognizant of their respective competitors are in big trouble in today's challenging business climate. And thus, to create an edge over your competition in the initial stages of business, it might be a good idea to sacrifice short-term profits for traction, growth, and sales."

# Michael J. Palumbo
# My Story

One of my first great business successes was with my company, Third Millennium Trading, at the Chicago Board Options Exchange, which I started in 1996. Twenty years ago, back then computers had just begun to be used in a meaningful way in trading. What I identified was the need for quicker trade execution and deeper (more liquid) options markets.

Basically what I figured out was that there was a strong need for a “one-stop options shop” for the entire U.S. Stock Market. There were other companies doing this, but getting an actual trade done was sometimes a slow process, especially when there was a lack of liquidity.

I identified the need to shorten the amount of time it took to get a trade done, while also providing more liquidity than other firms across the entire U.S. equity options market.

Trading was not actually done on computers at this time, at least not like today. I figured out a way to evaluate risk very quickly, which allowed my firm to respond to trade requests in seconds, while other firms were taking minutes. This may not sound like a big difference, but in trading every second is crucial. Today, trading is done in milliseconds, and the game has changed. But in the late 1990’s and early 2000’s my innovation within U.S. options trading allowed my company to become one of the largest U.S. options and equities trading firms in America (if not the world) in a very short period of time.

I was also able to create over 100 million dollars in wealth by innovating the concepts of speed and depth within options markets. But it all began by first identifying a need, and then figuring out a way to fulfill that need.